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SUBJECT: EL SALVADOR TO ISSUE $800 MILLION IN EUROBONDS IN OCTOBER

¶1. (SBU) SUMMARY. The Government of El Salvador (GOES) announced plans to sell $800 million in Eurobonds in the international market in October. Proceeds from the Eurobonds will be used to improve the liquidity of public finances and provide funding for new social programs. While a new bond offering was expected to address El Salvador's debt issues, the move to issue new bonds this year, following two rating agency downgrades, comes as a surprise. Lower-rate loans from international institutions had been expected to get the GOES through the first half of 2010. End summary.

¶2. (U) The GOES announced plans to place $800 million in Eurobonds on the Luxembourg stock market in October. President Mauricio Funes stated that the bond emission is needed to provide liquidity to public finances and to invest in new social programs. These bonds form part of $1.8 billion in new debt the National Assembly authorized in May. Doctor Carlos Acevedo, President of the Central Bank, said he plans to place the remaining $1 billion in bonds sometime in 2010.

¶3. (U) The bonds, denominated in dollars, will have a seven year term with an interest rate between 7-8 percent. The GOES placed an ad in the Wall Street Journal in late August soliciting an investment bank and/or law firm to manage the actual emission, while the Central Bank will act as the financial agent. Flor Ivania de Fernandez of the International Management Office of the Central Bank, who is in charge of managing the emission, stated that they have just initiated the placement and contract process.

¶4. (U) The GOES has over $2.7 billion in existing Eurobonds outstanding: $654 million due in 2011; $800 million due in 2023; $500 million due in 2023; $286 million due in 2034; and $1 billion due in 2035. According to the most recent official projections, the GOES's fiscal deficit will exceed 5 percent for the current year.

¶5. (SBU) COMMENT: While the GOES was expected to issue new Eurobonds before $654 million in existing bonds come due in 2011, the timing comes as a surprise. Since May, both Fitch and S&P have downgraded El Salvador's credit rating, citing the fiscal deficit and the effects of recession in both El Salvador and the US. Likewise, Moody's, which still has El Salvador at investment grade, announced September 14 that El Salvador was on the watch-list for a possible downgrade. The GOES had previously been negotiating additional funding from the International Monetary Fund, World Bank, and Inter-American Development Bank, which most Salvadoran economists had expected to get the GOES through the first half of 2010. Instead, the GOES is placing a new offering, at high rates comparable to less stable countries like Gabon, in an international market that may not yet have the stomach for new emerging market debt. END COMMENT.

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